

Message Text

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ACTION NEA-10

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SUBJECT: RESERVE BANK OF INDIA CREDIT POLICY FOR 1974-75 BUSY SEASON
(NOV 1, 1974 THROUGH APRIL 30, 1975)

FOLLOWING SENT ACTION NEW DELHI INFO CALCUTTA MADRAS
FROM BOMBAY NOV 01 REPEATED:

QUOTE

BOMBAY 2600

1. SUMMARY: THE RESERVE BANK OF INDIA HAS ANNOUNCED WZ
CONTROLLED CREDIT EXPANSION DURING NEXT SIX BUSY MONTHS. TWO
ELEMENTS OF THE CREDIT POLICY ARE THE AVAILABILITY OF RS 3.4
BILLION (\$453 MILLION) IN ADDITION TO RESOURCES FROM DEPOSIT
MOBILIZATION, FOR LENDING BY BANKS IN THE BUSY SEASON AND THE
PROVISION OF DISCRETIONARY ACCOMMODATION BEYOND THE LIMITS
INDICATED UNDER VARIOUS HEADS. PREFERENTIAL TREATMENT
IS TO BE ACCORDED TO PRIORITY OR CORE-SECTOR INDUSTRIES
IRRESPECTIVE OF SIZE BY LIBERALIZING CREDIT FLOW TO
THEIR NEEDS, WITH THESE EFFECTIVE ONLY FROM END-DECEMBER. ALTHOUGH
RESERVE BANK IS KEEN ON PREVENTING DECELERATION IN
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CORE SECTOR AND WAGEGOODS INDUSTRIES, IT MAY OPT FOR

AN EXPANSIONARY CREDIT POLICY AS THE BUSY SEASON
PROGRESSES PROVIDED THE PRICE SITUATION PERMITS SUCH A STEP.
END OF SUMMARY.

2. THE BUSY SEASON CREDIT POLICY WAS ANNOUNCED BY THE RESERVE BANK OF INDIA (RBI) GOVERNOR S. JAHANNATHAN IN BOMBAY ON TUESDAY, OCTOBER 29, 1974, AFTER A MEETING WITH HEADS OF MAJOR SCHEDULED COMMERCIAL BANKS. THE POLICY CHANGE IS IN LINE WITH THE INDICATIONS GIVEN BY GOI FINANCE MINISTER, C. SUBRAMANIAM, AT A MEETING IN DELHI LAST WEEK WITH BANK CHAIRMEN AND RBI GOVERNOR. THE RBI FEELS THAT CONTINUING INFLATIONARY PRESSURES LEAVE NO LATITUDE FOR EXISTING MONETARY RESTRAINT "AT THIS STAGE." "WE WILL WATCH AND TUNE THE CREDIT EXPANSION AS THE BUSY SEASON PROGRESSES", THE RBI GOVERNOR TOLD NEWSMEN. THE RBI HAS REFRAINED FROM ESTIMATING DEPOSIT GROWTH AND CREDIT EXPANSION DURING THE BUSY SEASON BECAUSE OF THE UNCERTAINTY OF MONETARY DEMAND BY GOVERNMENT AS WELL AS COMMERCIAL SECTOR, AND FLUCTUATING PRICES. ITS THINKING SEEMS TO BE THAT THE DEPOSIT GROWTH WILL BE BETTER AND CREDIT CREATION LESS PRONOUNCED THAN IN THE 1973-74 BUSY SEASON - WHEN DEPOSIT INCREASED BY RS 6.69 BILLION (\$892 MILLION) AND CREDIT EXPANDED BY RS 9.53 BILLION (\$1.3 BILLION).

3. RBI HAS STIPULATED STATUTORY LIQUIDITY RATIO UNCHANGED AT 33 PERCENT FOR THE BUSY SEASON AND HAS OFFERED LIMITED ASSISTANCE TO BANKS THROUGH REFINANCE, REDISCOUNTING OF BILLS AND RELEASE OF PART OF CASH DEPOSIT RESERVES MAINTAINED BY BANKS WITH THE RBI. THESE THREE SOURCES OF FINANCING ARE EXPECTED TO YIELD ABOUT RS 3.4 BILLION (\$453 MILLION) TO THE BANKING SYSTEM:

(1) THE MINIMUM STATUTORY CASH DEPOSIT RATIO FOR BANKS WOULD BE REDUCED FROM 5 TO 4 PERCENT. THE REDUCTION BEING IN TWO INSTALMENTS, 0.5 PERCENT WITH EFFECT FROM DECEMBER 14, 1974, AND FURTHER 0.5 PERCENT FROM DECEMBER 28, 1974. THIS IS LIKELY TO YIELD RS 1.2 BILLION (\$160 MILLION) TO BANKS BY END-1974. THE MINIMUM NET LIQUIDITY RATIO RELEVANT FOR LENDING BY RBI AT BANK RATE WILL BE REDUCED FROM 40 TO 39 PERCENT FROM DECEMBER 28, 1974, THE MAXIMUM RATE CHARGEABLE FOR REFINANCING REMAINING UNCHANGED AT 18 PERCENT.

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(11) BANKS' ORDINARY RECOURSE TO THE RBI FOR REFINANCE WOULD BE LIMITED TO AN AMOUNT EQUAL TO 1 PERCENT OF THEIR DEMAND AND TIME LIABILITIES AS ON SEPTEMBER 27, 1974. THIS WOULD ENABLE BANKING SYSTEM TO TAP RS 1.2 BILLION (\$160 MILLION) OF REFINANCE FROM RBI. BANKS WOULD ALSO BE GIVEN A "MODERATE" AMOUNT OF REFINANCE AGAINST FOOD PROCUREMENT ADVANCES IN THAT 50 PERCENT OF CREDIT EXTENDED TO PUBLIC FOOD

PROCUREMENT WOULD BE AVAILABLE WHEN THE OUTSTANDING FOOD ADVANCES CROSSED RS 3 BILLION (\$400 MILLION) MARK. AT RS 4.5 BILLION (\$600 MILLION), BANKS WOULD BE ELIGIBLE FOR FULL REFINANCE FOR THE INCREMENTAL AMOUNT.

(111) BILL FINANCE WILL BE MADE AVAILABLE BY RBI TO EACH BANK EQUIVALENT TO 10 PERCENT OF ITS TOTAL INLAND BILLS PURCHASED AND DISCOUNTED AS ON SEPTEMBER 27, 1974. THIS ACCOMMODATION AMOUNTING TO RS 1 BILLION (\$133 MILLION) FOR THE BANKING SYSTEM WILL BE AVAILABLE AT THE BANK RATE WITHOUT ADVERSE EFFECT ON NET LIQUIDITY RATIO OF BANKS.

THE RBI EXPECTS BANKS TO MAINTAIN CREDIT-DEPOSIT RATIO AT AROUND 71 PERCENT AT THE END OF 1974-75 BUSY SEASON.

4. A KEY ELEMENT OF THE CREDIT POLICY IS THE DISCRETIONARY ACCOMMODATION BY RBI OVER AND ABOVE THE LIMITS PRESCRIBED UNDER VARIOUS HEADS. REDISCOUNT ALLOWED ON DISCRETIONARY BASIS, (I.E. IN EXCESS OF THE BASIC QUOTA OF 10 PERCENT OF THE TOTAL INLAND BILLS PURCHASED AND DISCOUNTED) WILL BE AT A SPECIFIED REDISCOUNT RATE RANGING FROM 10 PERCENT TO 15 PERCENT PER YEAR. THIS FACILITY WILL BE EXCLUDED FROM DETERMINING

NET LIQUIDITY RATIO OF BANKS.

5. THE BROAD STRUCTURE OF SELECTIVE CREDIT CONTROL REMAINS UNCHANGED. RBI GOVERNOR HAS APPEALED TO BANKS TO BE MORE SELECTIVE IN CREDIT DEPLOYMENT TO SUSTAIN INVESTMENT, AUGMENT PRODUCTION AND FACILITATE BETTER DISTRIBUTION OF ESSENTIAL COMMODITIES. THE PRIORITY SECTOR INDUSTRIES INCLUDE AGRICULTURE, SMALL-SCALE INDUSTRIAL UNITS HAVING CREDIT LIMITS OF RS 1 MILLION (\$133,333) AND BELOW, PRODUCING WAGE GOODS (SMALL-SCALE UNITS UNCLASSIFIED

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PRODUCING INESSENTIAL GOODS ARE NO MORE GIVEN PRIORITY), EXPORT-ORIENTED INDUSTRIES AND "CORE" SECTOR COMPRISING OF FERTILIZERS, PESTICIDES, AGRICULTURE AIDING INDUSTRIES, TRANSPORT, ELECTRICAL EQUIPMENT, BASIC METALS AND MINERALS AND MASS-CONSUMPTION ORIENTED UNITS PRODUCING CONTROLLED VARIETIES OF CLOTH, EDIBLE OILS AND SUGAR.

6. JAHANNATHAN DENIED THAT THE CREDIT SQUEEZE HAS RESULTED IN SIGNIFICANT LESSENING OF CONSUMER DEMAND AND HE SAID THAT DEMAND IS THERE IF PRICES ARE RIGHT. HE HAS ALSO CLAIMED THAT PRODUCTION HAS NOT SUFFERED UNDER THE PRESENT CREDIT SQUEEZE.

7. THE BUSY SEASON CREDIT POLICY OF RBI, AS WE SEE IT, SEEMS A CAUTIOUS, GRADUAL EXPANSION OF CREDIT, WITH CONTINUOUS VIGIL

ON PRICE LEVEL. ALTHOUGH THE RBI GOVERNOR HAS RULED OUT CREDIT LIBERALIZATION DUE TO THE INFLATIONARY SITUATION, THERE IS A MARGINAL LOWERING OF CASH DEPOSIT REQUIREMENT WITH THE RBI. THIS REDUCTION, BEGINNING TOWARDS THE END OF THE YEAR IS PERHAPS DUE TO RBI EXPECTATION THAT CROPS WOULD MOVE INTO MARKET BY THAT TIME CAUSING DOWNWARD TREND IN PRICES. AT SUCH POINT, INJECTION OF MORE FUNDS INTO THE ECONOMY MIGHT NOT PROVE INFLATIONARY.

8. THE FACILITY OF REDISCOUNTING OF BILLS WITH THE RBI MIGHT MAKE AVAILABLE LESS AMOUNT TO BANKS THAN THAT OF THE BUSY SEASON LAST YEAR SINCE ANYTHING MORE THAN RS 1 BILLION (\$133 MILLION) WOULD BE OF A DISCRETIONARY NATURE. BILLS DISCOUNTED TOTALLED RS 2.8 BILLION (\$373 MILLION) AT THE END OF THE LAST BUSY SEASON. FZONED BANE
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